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In the Supreme Court of the United States

OCTOBER TERM, 1943

PACIFIC GAS AND ELECTRIC COMPANY, PETITIONER,

v.

SECURITIES AND EXCHANGE COMMISSION

Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

(With Appendix)

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Petitioner, Pacific Gas and Electric Company,[1] prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit (R 1776), which affirmed, by an equally divided court (R 1741), an order of the Securities and Exchange Commission (R 1932), denying Petitioner's application for an order, pursuant to Section 2(a)(8) of the Public Utility Holding Com-

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NOTE: All emphasis is supplied by us unless otherwise noted.

[1]For convenience Pacific Gas and Electric Company will be called Pacific Gas; the Securities and Exchange Commission, the Commission; The North American Company, North American; and the Public Utility Holding Company Act of 1935, the Act.

pany Act of 1935, declaring it to be not a subsidiary of The North American Company, a registered holding company.

OPINIONS BELOW

The decision in the Circuit Court of Appeals (six judges participating), affirming the order of the Commission by an equally divided court, and also the dissenting opinion, are reported in 139 F.2d 298. The prior opinions in the Circuit Court of Appeals (three judges sitting) are reported in 127 F.2d 378.[1] The opinion and order of the Commission dated September 10, 1941, is reported in 10 S.E.C. ....., Holding Company Act Release No. 2988.

JURISDICTION

The judgment of the court below was entered November 18, 1943 (R 1776). A timely petition for rehearing was filed, and was denied February 23, 1944 (R 1777), at which time the court *sua sponte* entered an order continuing in effect the stay of the order of the Commission theretofore granted and likewise staying its mandate until after this Court disposes of a petition for certiorari, if such petition be filed on or before April 10, 1944.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U.S.C. 347) and under Section 24(a) of the Public Utility Holding Company Act of 1935 (15 U.S.C. 79x).

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[1]The majority opinion in the court below on the first hearing is printed at page 15 of the Appendix hereto and the opinion on the rehearing at page 34 of the Appendix.

STATUTE INVOLVED

The statute involved is the Public Utility Holding Company Act of 1935 (49 Stat. 803; 15 U.S.C., Sec. 79-79z6) and particularly Sections 1, 2(a)(8) and 24 thereof, which are printed at page 1 of the Appendix.

This statute provides for Federal control of public utility holding companies, and their eventual elimination, and brings under such control not only the holding companies, but also their subsidiary operating companies.

Section 2(a)(8) provides that any company 10% or more of whose voting stock is owned by a holding company is a subsidiary thereof unless the Commission by order declares it not to be a subsidiary; and requires the Commission to declare it not to be a subsidiary if, on application by the company, the Commission finds that it is not controlled by, and that its management or policies are not subject to, the controlling influence of the holding company.

QUESTIONS PRESENTED

The questions here are:

(a) Whether the Commission properly interpreted and applied the Act in denying the application of Pacific Gas to be declared not to be a subsidiary of North American (owner of 17.71% of Pacific Gas voting stock), irrespective of whether in fact Pacific Gas is subject to its controlling influence.[1]

[1]It has never been contended that Pacific Gas is controlled by North American or is an intermediary. The only issue considered by the Commission is whether Pacific Gas is subject to the "controlling influence" of North American under clause (iii) of Section 2(a)(8) (R 1887-9). The Commission did not find that such influence existed.

(b) Whether the court below afforded the judicial review of the Commission's order required by Section 24 of the Act when it affirmed the order by an equally divided court.

Petitioner Contends

1. A local utility is not subject to regulation under the Act as a subsidiary of a holding company unless it is in fact controlled by or is subject to the controlling influence of such holding company.

The Commission here misconstrued and misapplied the Act in holding Pacific Gas to be a subsidiary of North American, irrespective of whether in fact it is subject to North American's controlling influence. Its order is based on its finding that North American as owner of 17.71% of the stock of Pacific Gas "has the power—if the occasion arises and if it so desires—to make its influence felt in a substantial and affirmative manner" (R 1922). It held that the mere possibility of such influence amounted to the *controlling* influence required by the Act, and construed the Act as presumptively requiring that Pacific Gas be regulated unless "excepted" (R 1931).

Admittedly there have never been any intercorporate transactions between these companies, and North American has made no attempt to exert any controlling influence over Pacific Gas (R 1920). There was no substantial evidence from which the existence of a controlling influence could be inferred, and there is ample evidence of its non-existence.

2. There is no substantial evidence of the existence of a controlling influence of North American over Pacific Gas.

3. The court below erred (a) in affirming the Commission's order by an evenly divided court, thus denying the review provided in the Act and (b) by leaving in effect and failing to set aside the order of the Commission which is based upon a misconstruction of the Act, and is unsupported by evidence.

STATEMENT OF THE CASE

The Statute

The pertinent portions of the Act are printed in the Appendix, pages 1-14. Section 2(a)(8), which prescribes the procedure for determining whether or not a local utility is a subsidiary of a holding company, will be found commencing at page 7 of the Appendix.

As indicated by its title (Public Utility Holding Company Act of 1935), the Act was passed to meet the problems and eliminate the evils attributed to interstate public utility holding companies. These evils (recited in Sec. 1, Appendix, p. 1) arise from ineffective state regulation and transactions between holding companies and their subsidiaries not carried out at arm's length. As stated in the Senate Report on the bill (No. 621, 74th Congress, First Session, page 4):

> "This title is concerned only with holding companies in the public utility field, defined for the purposes of the title as companies which control operating public-utility companies."

The Act was not designed to regulate any local utility as such, but "only when its corporate and financial activities became inextricably involved with the holding company which controls it. The limited authority of the Commission over an operating company exists only to the extent necessary to control intercorporate financial relationships within an interstate holding-company system. * * * The Commission has no authority over an independent operating company and no authority over an intrastate holding-company system which is independent and not under the control of a super-holding company outside of the state." (Page 9 of Appendix A to the Commission's brief in *Electric Bond & Share Co. v. S. E. C.*, 303 U.S. 419.)

The test of whether a local public utility is or is not under the Act, is whether it is in fact "controlled by", or whether its "management or policies" are subject to the "controlling influence" of the holding company (Sec. 2(a)(8)—Appendix, p. 7).

The machinery for the determination of this jurisdictional fact of "control" or "controlling influence" is this: if less than 10% of the voting stock of the local utility is owned by the holding company, then the local company is not deemed a "subsidiary" and subject to regulation unless the Commission initiates a proceeding and, after hearing, finds that it is controlled by or subject to the controlling influence of the holding company; on the other hand, if 10% or more of the voting stock of the local utility is owned by the holding company, then the local utility is deemed to be a subsidiary, unless the Commission finds that it is not subject to the control or controlling in-

fluence of the holding company, and it is provided that the Commission *shall,* on application, declare it not to be a subsidiary upon proof that it is not controlled by or subject to the controlling influence of the holding company.

Ownership of 10% of a local utility's stock has significance only as marking the point where the Commission or the utility is placed under the duty of initiating proceedings for a determination of status. Senator Wheeler, in charge of the bill, pointed this out during the debate when he said (79 Cong. Rec. p. 6397):

> "This is only prima facie evidence; but even if they hold 40 percent of the stock of a company they may come before the Commission and produce evidence that they are not actually in control of the company, and the Commission is directed to make a finding and to exempt them if they are not actually controlling the company as the word 'control' is defined in the bill."

See also Senator Wheeler's remarks at 79 Cong. Rec. p. 8439, where he said:

> "The mere ownership of the 10 percent of the stock does not of itself make him a holding company, because unless he actually controls the company he is not a holding company."

The existence of control or controlling influence is to be determined as of the time of the inquiry. The Act speaks in the present tense and requires findings that the management and policies "are" subject to the controlling influence of the holding company. The Act, moreover, contemplates that a future possibility

of a controlling influence shall not be the basis for denial, since it provides that the Commission may require periodic renewal of the order, the rendition of reports or other safeguards which it finds "necessary or appropriate to ensure that in the case of the applicant the conditions specified * * * are satisfied during the period for which such order is effective" and it may revoke the order whenever it finds that such conditions are not satisfied (Sec. 2(a)(8), Appendix p. 7).

It is clear that Congress did not intend that 10% owned local utilities should be regulated under the Act unless "excepted" by the Commission, or that the statute "presumptively requires" that a 10% owned local utility be regulated under the Act as a subsidiary, as was held by the Commission in this case.

The foregoing cannot be more succinctly stated or the rationale of the Act more clearly expounded, than in the following passage quoted from page 195 of the brief of the Commission in this Court in the *Electric Bond and Share* case (303 U.S. 419) in which case the Act was held constitutional.[1] While the discussion there refers to "control" from the standpoint of the holding company, the statutory provision with respect to "control" from the standpoint of the sub-

[1]This brief is signed by Homer Cummings, Attorney General, Allen E. Throop, General Counsel, Securities and Exchange Commission, Robert H. Jackson, then Assistant Attorney General, and by Benjamin V. Cohen and Thomas G. Corcoran, Special Assistants to the Attorney General and recognized authors of the bill.

sidiary is similar, and the discussion is equally applicable:

> "The bill as originally introduced defined a holding company as a company which directly or indirectly controls a public-utility company. As thus drafted the bill would have made it necessary for a company to determine for itself and at its own risk whether it had such a controlling authority over a utility company as to constitute it a holding company. Had this provision not been changed or had it taken the slightly modified form suggested by the Committee of Public Utility Executives, holding companies would have had to guide their own action on the basis of a standard no more definite than that given to the Commission to guide its administrative determinations. Anyone familiar with modern corporate affairs knows the practical difficulties involved in determining the existence or non-existence of corporate control, one of the most elusive problems in corporate finance. There is no single, inflexible rule (whether it be stock ownership, interlocking directorates, or interlocking banking arrangements) that will give the correct solution in all cases. Those practical difficulties were brought out clearly in the testimony before the Congress of counsel for the Committee of Public Utility Executives (Hearings before the Committee on Interstate Commerce, United States Senate, 74th Congress, 1st Session, on S. 1725, p. 423) and in the testimony of counsel for the defendants (Id. at 326-327). The Congress in reliance upon the Sherman Act precedents (*Nash v. United States,* 229 U.S. 373) might have left the bill as it was originally drafted. Had it done so it might have

taken many years and successive decisions of this Court to determine just what companies are and which are not holding companies. The result would have been as unsatisfactory to the holding companies as to the public, and there would have been the further danger that the provision might be held invalid for indefiniteness. Cf. *United States v. Cohen Grocery Co.*, 255 U.S. 81. But a standard too vague to support a self-operating provision enforced by criminal liability may well state a policy and purpose sufficiently definite to serve as an appropriate standard for the guidance of administrative action. *Highland v. Russell Car & Snow Plow Co.*, 279 U.S. 253; *Continental Baking Co. v. Woodring*, 286 U.S. 352, 368.

"The standard of 'control' was known to be susceptible of judicial and quasi-judicial determination. It had been adopted by the courts themselves in some of the Sherman Act cases. *United States v. Union Pacific R. Co.*, 226 U.S. 61. The Congress, however, found it impracticable to put upon the Commission the burden of making the initial specific determination of control for each and every holding company before that company could be deemed a holding company and required to register. Not only would such procedure have been too cumbersome and dilatory to be effective, but it would have placed the burden of proof upon the Commission to ferret out elusive and subtle facts peculiarly within the knowledge of each company, an almost impossible task.

"The Congress selected the element of stock ownership, the factor most usually indicative of control, as *prima facie* evidence of control. And in the same provision the Congress set up the

machinery for rebutting this presumption so that a company may readily prove, if such be the fact, that it does not possess control. Such burden of proof is not onerous, because every company has completely within its own organization full knowledge and control of all the facts and evidence. And the Act provides that upon the mere filing in good faith of an application for exemption the company shall automatically be exempted until the Commission acts upon the application. Judicial review is provided to guard against any arbitrary action on the part of the Commission and to afford a remedy should the Commission's findings of fact be not supported by substantial evidence (Section 24(a)). No more careful and painstaking effort to meet every legal and practical requirement involved in this difficult and complicated situation could have been made by a legislative body.'"[1]

The Act clearly shows the intent of Congress that local utilities shall not be subject to the Act unless part of a holding company system; that the jurisdictional fact is whether or not the local utility is, at the time of the inquiry, in fact controlled by or subject to the controlling influence of the holding company; and that the presence of a 10% stock ownership is only a procedural device to set in motion an inquiry for the determination of the jurisdictional fact and is not of itself substantial evidence of the existence of such controlling influence.

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[1]See Senate Committee Report on the Bill (74th Congress, First Session, Report 621, page 5; also *Electric Bond and Share Co. v. S. E. C.* (C.C.A. 2) 92 F.2d 580, 592.

Pacific Gas a Local Utility

Pacific Gas distributes gas and electricity in California, where all of its properties and business are and always have been located. Incorporated in California in 1905, its properties include those of many predecessor companies, some of which were started in the 1850's to supply water and power to the gold mines. Its office is and always has been in San Francisco and its Board of Directors has never held a meeting elsewhere.

When the Act was adopted, North American owned 17.71% of the voting stock of Pacific Gas. This stock was issued to North American in 1930 by Pacific Gas in payment for certain utility properties in California theretofore controlled by North American, the purchase of which had long been planned by Pacific Gas. The purchase and the payment in stock was authorized by the California Railroad Commission.

When the purchase was made, Pacific Gas, realizing that the stock issued in payment would make North American its largest single stockholder, demanded and received assurances from North American that it would not attempt to interfere with its management or policies, or increase its holdings. It was also agreed that North American might nominate three out of fifteen directors, the number it could elect by exercise of its cumulative voting rights under California law, and also that one of these directors would be named to the Executive Committee consisting of five members. At the time of the hearing there were only two directors named by North American on the Board of Pacific Gas, neither of whom was on the Executive

Committee and neither of whom had attended any Board meetings.

There have never been any transactions of any kind between the two companies since North American received Pacific Gas stock in payment for its properties. It is also admitted that none of the relationships so often present between holding companies and operating companies in which they owned stock, were present or had ever existed here; there were admittedly no contracts, no exchange of operating information, no loans or financial transactions, no engineering, construction, accounting or other services, no common attorneys, and no banking or investment connections.

Proceedings Before the Commission

In November 1935, Pacific Gas filed its application under Section 2(a)(8), seeking a declaration that it is not a subsidiary of North American. The filing of this application exempted Pacific Gas from the Act until it should be disposed of. Five years later the matter was assigned for hearing before a trial examiner, which hearing commenced November 12, 1940, and concluded January 16, 1941.

Every director and principal officer of Pacific Gas was examined, and except for the two directors nominated by North American, all testified that they were not and could not be influenced by North American. The directors nominated by North American testified that that company held the stock of Pacific Gas solely as an investment and they had not attempted to, and did not think they could, influence its management or policies. The remaining directors, thirteen in number,

were made up, five of principal officers of the company and eight outstanding California businessmen, some of whose fathers had been founders of predecessor companies. All owned or were associated with the owners of substantial amounts of stock.

Upon invitation of the Commission, the California Railroad Commission appeared and participated. It showed that under the California Public Utility Act, Pacific Gas, since 1912, has been subject to its regulation, which covers all phases of its activities, including the issue of securities, rates, service, etc. and that it had been before the Commission in more than 900 proceedings. The Railroad Commission's statement (R 1875), concluded:

> "* * * we are aware of no instance during the course of this Commission's regulation of Pacific Gas and Electric Company when its management or policies appear to have been either controlled or influenced by North American Company. We may add that we perceive no public interest existing within the State of California, either for the protection of investors or consumers, which compels the conclusion that applicant, Pacific Gas and Electric Company, should be declared subject to the obligations and duties imposed by the federal Holding Company Act upon subsidiary utility corporations."

Following the hearing, the Commission's Trial Examiner filed a report (R 1779), recommending the granting of the application, and containing comprehensive findings of fact. He found that there had never been any inter-company transactions of any

kind between Pacific Gas and North American since the latter became a stockholder, and that Pacific Gas was not controlled by nor were its management or policies subject to the controlling influence of North American.[1]

The Commission, on September 10, 1941, denied the application. The basis of its decision is apparent from the following passages in its opinion (R. 1883):

> "There is almost no dispute as to the facts in this case as they are set forth in the trial examiner's report and in the briefs of both counsel. The point of issue with respect to the application under Section 2(a)(8) is rather one of statutory interpretation and in this respect we cannot agree with the conclusions reached by the trial examiner." (R 1912)

The opinion also states that:

> "We agree with the finding of the trial examiner that the record does not reveal any past attempts by North American to interfere affirmatively with the management or policies of PG&E." (R 1920)

Again the opinion says:

> "But our decision herein is based primarily on our finding that North American has the power—if the occasion arises and if it so desires—to make its influence felt in a substantial and affirmative manner." (R 1922)

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[1]These findings are printed at page 1779 of the Transcript and cover all essential facts. As pointed out in the Commission's opinion (R 1912), the Commission does not dispute them.

The opinion concluded with the following statement:

> "The only question which we have decided is that, in the circumstances of this case where the statute presumptively requires that PG&E be regulated as a subsidiary of North American, the facts in the record before us do not demonstrate that PG&E is entitled to be excepted from the general requirement of regulation as a subsidiary of a registered holding company." (R 1931)

The Proceedings in the Court Below

In the first decision of the court below, three judges sitting, Judge Haney, with Judge Stephens concurring, approved the Commission order. Judge Garrecht dissented (R-1718).

The majority opinion, while saying "that a reasonable man could reach the conclusions the Commission reached and therefore the finding[1] must be sustained", finally turned upon the proposition that under clause (iii) of Section 2(a)(8), the Commission had uncontrolled discretion to subject a local utility (10% of whose stock was owned by a holding company) to regulation under the Act if it believed it was in the public interest to do so, irrespective of any evidence. The court reached this remarkable conclusion by construing Section 2(a)(8) as containing four conditions instead of three, the fourth condition being termed the "necessity clause", which, being independent of the control or controlling influence clauses, authorized the Commission to dismiss an application if it believed

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[1]The "finding" was only that Pacific Gas had not *demonstrated* the absence of controlling influence or the future possibility of any influence.

that it was in the public interest to hold the local utility subject to regulation under the Act. (Appendix pp. 29-33)

This novel construction of the Act had never before (nor has it since) been advanced by the Commission or by any court, and the Commission's counsel made no attempt to sustain it.

A rehearing before the entire court, then consisting of seven judges, was granted (R 1739). On rehearing the court affirmed the order of the Commission, by an equally divided court, Judge Haney having died in the interim.

The court below entered its order without any expression other than that its action was "by an evenly divided court" (R 1741).

Judge Garrecht, however, filed a dissenting opinion from the judgment affirming the Commission's order, in which dissent Judge Mathews joined. (Appendix, p. 34) This dissenting opinion contains an extensive analysis of the record before the Commission, and finds that there was no substantial evidence of the existence of a controlling influence by North American over Pacific Gas; that the Commission's findings rested on speculation and conjecture as to whether North American might acquire a controlling influence in the future; that the Commission misinterpreted the Act by holding that susceptibility to future influence was the equivalent of the controlling influence required by the Act.

Judge Garrecht characterizes the Commission's treatment of the evidence as follows:

> "To reach the conclusion arrived at by the Commission every circumstance is viewed with a hostile eye and every instance tortured into some semblance of sinister purpose. * * *" (Appendix p. 51)

Again, Judge Garrecht says:

> "There are other instances where the Commission very frankly has interpreted the testimony of the witnesses contrary to their evidence. These interpretations, which are exaggerated into some semblance of an argument, are then designated as inferences of the Commission as to 'events which might happen' but 'not what actually happened'." (Appendix pp. 53-54)

He also says:

> "It is also clear that the vague, artificial tests here employed are not sanctioned by the Act. Nor was it expected that inferences based upon inferences, or suppositions, or even possibilities, would be substituted for substantial evidence." (Appendix p. 63)

The opinion concludes with this statement:

> "To sustain the Commission on the record here would require us to hold, as the court did on the first hearing, that its determination of what is necessary in the public interest is a matter within the uncontrolled discretion of the Commission. This is not the proper interpretation of the statute and counsel representing the Commission do not so contend." (Appendix p. 67)

REASONS FOR GRANTING THE WRIT

The questions here presented are important questions in the interpretation and administration of the

Act. None has heretofore been settled by this Court. Despite the requirement of the Act that orders of the Commission shall be subject to judicial review on petition of an aggrieved party, we shall be deprived of such review unless this Court grants the writ here sought.

These questions are admittedly different from those involved in any of the other cases under Section 2(a)(8) of the Act. An examination of all cases which we have been able to find involving this section, reveals that in every case where the Commission found the local utility to be a subsidiary of a holding company, it had in fact been actually controlled or subjected to a controlling influence, and there had been intercompany transactions—conditions admittedly not present here.

On the first hearing in the court below, the majority opinion sought to sustain the order by a completely novel construction of the Act, under which the Commission, on its own concept of the public interest, regardless of whether or not its finding was sustained by evidence, could subject a local utility to federal regulation.[1]

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[1]In granting the rehearing, the court below characterized its opinion as follows:

> "In the above entitled case this Court (three judges sitting, two judges agreeing, one dissenting) has announced a construction of the Securities and Exchange Act which, if adhered to, will have an important and far-reaching effect upon the administration of the Act"

and pointed out "our construction of the Act was not intimated in either brief or in the oral argument" (R 1739).

On rehearing, the court below affirmed the Commission's order by an equally divided court without any expression whatever of the views of those judges who favored affirmance of the order, although it is fair to assume they did so on the grounds set forth in the first opinion, which, as the court pointed out, involved a construction of the Act not urged by the parties, and which if adhered to would have "far-reaching effect on the administration of the Act". Two of the judges joined in a dissenting opinion in which the absence of any substantial evidence justifying denial of the application was forcefully pointed out.

There are now printed in the official reports: (1) the opinion of the Commission; (2) the affirming and dissenting opinions of the court below on the first hearing; (3) the order of the court below affirming by an even division; and (4) the dissenting opinion on rehearing.

Unless this Court grants the writ, there will have been no review of the order, and these conflicting interpretations and applications of the Act will be a source of confusion, leaving both the Commission and all affected companies in uncertainty as to its true meaning. It is submitted that the serious but unresolved questions involved in the interpretation of this important federal statute, should be settled by this Court.

The Commission Misconstrued and Misapplied the Act.

The Commission erroneously construed the Act as empowering it to exercise control over a local utility

even though it does not find that the utility is either controlled by or subject to the controlling influence of a holding company and where the evidence not only does not support such a finding but abundantly supports a contrary finding.

There is no dispute as to the facts. The Commission said that "There is almost no dispute as to the facts in the case as they are set forth in the trial examiner's report and in the briefs of both counsel. The point of issue with respect to the application under Section 2(a)(8) is rather one of statutory interpretation and in this respect we cannot agree with the conclusions reached by the trial examiner" (R 1912).

The Commission said the point at issue was one of statutory interpretation. This issue is—which of these two interpretations of the Act is correct?

Our interpretation is that a local utility is only subject to the Act if in fact controlled by or subject to the controlling influence of the holding company at the time of the hearing; that the proceeding before the Commission to determine this jurisdictional fact is quasi judicial in character and the issue is to be decided on the record at the hearing; that the application cannot be denied if the evidence shows the nonexistence of control and controlling influence; that if the Commission believes that a controlling influence *might* arise in the future, though not present at the time of the hearing, it cannot deny the application, but

must issue a conditional order as provided in the Act.[1]

The Commission's interpretation is that a 10% owned local utility is "by definition" a subsidiary and subject to Commission regulation unless "excepted" by the Commission, and the Commission may, as it did in this case, deny the application, even though the existence of control or controlling influence is not found, and cannot be found on the evidence—if it believes that at some future time the holding company may exert a substantial influence. The Commission's view as expressed in its opinion is: "The only question we have decided is that, in the circumstances of this case where the statute *presumptively requires* that PG&E be regulated as a subsidiary of North American, the facts in the record before us do not *demonstrate* that PG&E is entitled to be *excepted* from the general requirement of regulation as a subsidiary of a registered holding company" (R 1931).

The Commission's misconstruction of the Act infects its entire order. Admitting that North American had never controlled or exerted a controlling influence over Pacific Gas, and that there had never been any intercompany transactions, the Commission nevertheless denied the application solely because of its belief "that North American has the power—if the occa-

[1]We do not contend, as the Commission frequently erroneously suggests we do, that the "controlling influence" must be exercised in order to meet the statutory requirement. For the purposes of this case, we concede that the present existence of the power, whether or not actually being exercised, is sufficient. The power, however, must be "controlling" and not something less then controlling.

sion arises—and if it so desires, to make its influence felt in a substantial and affirmative manner".

The question presented on this phase of the case is not whether the Commission's order might have been sustained had it properly pursued its statutory authority. The question is, what did the Commission do, and did it properly construe and apply the Act?

The Commission did not find from the evidence that any controlling influence existed. It merely said that it was not convinced that Pacific Gas had demonstrated the absence thereof. This is attributable entirely to its belief that it could deny the application, regardless of the absence of evidence of the existence of a controlling influence, if it thought that there was a possibility of *any* influence being exerted in the future.

An ultimate finding of the Commission, couched more or less in the statutory language, must be disregarded where, as here, it appears from the entire opinion that the Commission, in fact, reached its conclusion upon a mistaken view of its statutory powers.[1]

Where the Commission has misconstrued its statutory authority and based its action upon such misconstruction, it is immaterial whether the order might have been sustained by substantial evidence had the Commission properly pursued its statutory authority. In *Securities and Exchange Commission v. Chenery Corp.*, 318 U.S. 80, 93, this Court held:

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[1] *Southern Pacific Co. v. Interstate Commerce Commission*, 219 U.S. 433, 449; *Passenger Scrip Case*, 263 U.S. 603, 611; *Ann Arbor R.R. Co. v. U. S.*, 281 U.S. 658, 665; *Anchor Coal Co. v. U. S.*, 25 F.2d 462, 464.

"Judged, therefore, as a determination based upon judge-made rules of equity, the Commission's order cannot be upheld. Its action must be measured by what the Commission did, not by what it might have done. It is not for us to determine independently what is 'detrimental to the public interest or the interest of investors or consumers' or 'fair or equitable' within the meaning of §§ 7 and 11 of the Public Utility Holding Company Act of 1935. The Commission's action cannot be upheld merely because findings might have been made and considerations disclosed which would justify its order as an appropriate safeguard for the interests protected by the Act. There must be such a responsible finding. Compare *United States v. Chicago M., St. P. & P. R. Co.*, 294 U.S. 499, 510-11. There is no such finding here."

That the Commission misconstrued and misapplied the Act is further shown by the following:

1. It imposed upon Pacific Gas the virtually impossible burden of "demonstrating" a negative, i.e., that a controlling influence did not exist.

The Commission said:

"First, it is clear that the application herein cannot be granted unless we can find that applicant has sustained the burden of *demonstrating* that its management and policies are not subject to the controlling influence of North American" (R 1912).

"* * * We hold that applicant has not *demonstrated* that its management and policies are not subject to the controlling influence of North American * * *" (R 1930).

> "* * * The facts in the record before us do not *demonstrate* that PG&E is entitled to be excepted from the general requirement of regulation as a subsidiary of a registered holding company" (R 1931).

This requirement of proof to a demonstration should be contrasted with the statements of those who spoke in Congress in favor of the enactment of the statute, and of Commission counsel who successfully argued in this Court in support of the constitutionality of the Act. The latter referred to the presumption as one "which might be rebutted", as one under which a company may "readily prove absence of control" and as one which "can readily be rebutted * * * upon a showing that the company does not in fact exercise control".

Particularly where it is required that the parties subject to the burden of proof establish a negative convincing proof is not required, let alone demonstration. All that is required is that the proof be sufficient to show that the negative fact or circumstance is probable. 20 Am. Jur. 1099; *Prentice v. Crane,* 234 Ill. 302, 84 N.E. 916; *Baltimore etc. R. Co. v. United States,* 298 U.S. 349, 378.

2. It treated the procedural provision of the Act governing the initiation of proceedings for determination of status as evidence to be given weight and effect as against undisputed evidence that Pacific Gas is not in fact subject to the controlling influence of North American. It converted a procedural rule into a dec-

laration of substantive law; and treated the procedural device as evidence.

A presumption does not have a quality of affirmative evidence. *Del Vecchio v. Bowers,* 296 U.S. 280; *Meeker v. Lehigh Railroad,* 236 U.S. 412, 430; *Mobile etc. R. Co. v. Turnipseed,* 219 U.S. 35; *Western R. Co. v. Henderson,* 279 U.S. 639.

It is well settled that a presumption cannot be weighed as evidence against direct evidence to the contrary. *New York Life Ins. Co. v. Gamer,* 303 U.S. 161; *Tot v. United States,* 319 U.S. 463; *Commercial Corp. v. New York Barge Corp.,* 314 U.S. 104.

3. It treated an ownership of 17.71% of the voting stock as being, in and of itself, sufficient ground for denying the application.

While a 10% stock ownership may be evidence to be given appropriate weight, it seems clear that Congress could not have intended that, by itself, it would be deemed to constitute sufficient basis for denying an application. Otherwise the provision for judicial review is meaningless, since the very fact giving rise to the inquiry would itself preclude reversal of the Commission. This is recognized in the Commission's brief in the *Electric Bond & Share* case, supra, page 8, where it is said that:

> "Judicial review is provided to guard against any arbitrary action on the part of the Commission and to afford a remedy should the Commission's findings of fact be not supported by substantial evidence."

4. It construed the words "subject to controlling influence" used in the Act as meaning "susceptible to

domination". (See Judge Garrecht's opinion, Appendix p. 61.)

5. It held that the fact that North American's stock would enable it "to make its influence felt in a substantial and affirmative manner" and would make it a "formidable opponent" in a proxy fight amounted to controlling influence.

6. It held that a mere possibility of future control was sufficient ground for denying the application.

Even if the Commission Did Not Misconstrue and Misapply the Act, the Order Should Be Set Aside Because Not Supported by Substantial Evidence.

As pointed out, the Commission misconstrued and misapplied the Act, and not having followed its statutory authority, the order should be set aside.

But even if it had followed its statutory authority, the order should be set aside because not supported by substantial evidence.

We assert that there is no evidence of record from which a reasonable person could conclude that a controlling influence existed. We go further and assert that the Commission's failure to make such a finding was because it did not believe that the evidence would justify such a conclusion. Judge Garrecht's opinion so clearly shows that there was no substantial evidence of controlling influence that we will not further deal with the point but request this Court to examine Judge Garrecht's opinion—Appendix p. 34.

Indeed it seems clear from Judge Haney's opinion on the first hearing (Appendix p. 15) that he would

not have upheld the order except for his erroneous view that the Act contained a fourth requirement, i.e. the necessity clause, which empowered the Commission to deny the application even if a controlling influence was shown not to exist, if the Commission believed such was in the public interest, a construction never before or since announced by the Commission or by any court. It is reasonable to suppose, in the absence of a further opinion, that the judges who favored affirmance on rehearing did so on the same grounds.

While Commission orders under Section 2(a)(8) have been reviewed in four other cases,[1] the facts here, summarized in earlier pages and shown in detail in the opinion of Judge Garrecht, are entirely different from those in any of these cases.

The circumstances to be considered in ascertaining whether a controlling influence exists are set out in *American G. & E. Co. v. S. E. C.* (C.C.A. D.C.), 134 F.2d 633, 642. The opinion in that case was by Mr. Justice Rutledge, who said:

> "The existence of 'controlling influence' is a factual determination to be ascertained in the Commissioner's expert judgment by the weighing of circumstantial evidence and the drawing of reasonable inferences therefrom. The principal factors in determining this from the special cir-

[1] *Detroit Edison Co. v. S. E. C.* (C.C.A. 6) 119 F.2d 730; *Hartford Gas Co. v. S. E. C.* (C.C.A. 2) 129 F.2d 794; *Public Service Co. of N. J. v. S. E. C.* (C.C.A. 3) 129 F.2d 899; *American G. & E. Co. v. S. E. C.* (C.C.A. D.C.) 134 F.2d 633.

cumstances of each case for the statutory exemption are the size and extent of the companies involved, the extent of the intercompany relationships, the ownership and distribution of securities, and the parent company's part in the organization and development of the subsidiary company together with the past relationships and, because of the public interest and purposes of the Act involved, consideration must be given to the relationship of charges between the two companies for financing, service and construction contracts, etc."

In that case and also in the *Detroit* and *Public Service Company of New Jersey* cases, the utility had been organized under the auspices of the holding company. There was a long history of affiliation of a majority of the utility's directors and officers with the holding company. The holding company had participated in underwriting the utility's securities. There were management contracts, joint purchasing arrangements, common offices, and many of the other intercorporate transactions which the Act sought to regulate. In the *Hartford* case, while the past historical connections of the company were not shown to have been as extensive as in the other cases, there was an indirect underwriting of securities by the holding company and the purchases of gas accounting for nearly 60% of the utility's operating expenses from a recognized affiliate of the holding company.

Here, on the other hand, there have never been any of these intercorporate relationships. The Trial Examiner's findings of fact in this regard, which were

approved by the Commission, and which are recited in Judge Garrecht's opinion (Appendix p. 59), are as follows:

> "There have been no contracts between Applicant and North American or its subsidiaries except the contract dated March 29, 1930. (The agreement by which PG&E acquired the properties of North American in California.)
>
> "Neither North American nor any of its affiliates or employees has ever performed any services with or without charge, for Applicant.
>
> "There has been no exchange of operating information between the Applicant and the admitted subsidiaries of North American.
>
> "There have never been any intercompany loans or financial transactions between the Applicant and North American or its subsidiaries.
>
> "All of Applicant's major acquisitions and construction projects have been and are decided upon, budgeted and carried out within the PG&E organization and entirely independent of North American at all stages.
>
> "North American's organization has never assisted Applicant in the preparation of any Registration Statements, nor has its Secretarial Department ever assisted Applicant in any manner.
>
> "Applicant and North American do not employ the same accountants, attorneys or engineers.
>
> "Applicant does not employ any former officers or employees of North American, with the exception of Mr. Black, and with the exception of those who were officers or employees of acquired companies at the time of their acquisition. North

American has never recommended or suggested to Applicant the employment of any person or been asked its views thereon.

"No employees of Applicant, nor of North American or of its admitted subsidiaries have ever been loaned by either to the other."

In the last analysis the Commission's denial of the application rests solely on the ownership by North American of 17.71% of Pacific Gas stock, the very fact which gives rise to the proceeding before the Commission.

The Court below did not give the Review contemplated by the Act.

The proceeding in the court below being an original proceeding by virtue of Section 24(a) of the Act, it was error for the court to affirm the order of the Commission by an equal division. The effect of such affirmance is to deny the judicial review to which, by the statute, the parties are entitled.

In *Durant v. Essex Company* (1868) 7 Wall. 107, this Court held that affirmance of an appeal by an equally divided court decided nothing except that the case was closed and was equivalent to dismissal of the appeal.

Section 24(a) imposes a positive duty on the Circuit Court of Appeals to determine the questions arising out of a petition to review an order of the Commission. The section provides that upon the filing in the Circuit Court of Appeals of a transcript of the record before the Commission "such court shall

have exclusive jurisdiction to affirm, modify or set aside such order in whole or in part". The power of the Commission itself is lost during the pendency of the proceeding and the court is bound to decide the controversy.

In an original proceeding before a court made up of more than one judge, concurrence in a decision by a majority of the court is essential to any action. If such concurrence cannot be obtained, the matter must remain in *statu quo,* in the absence of some provision such as formerly existed in connection with the Circuit Courts of the United States, when, on a division of opinion, the matter could be certified to a higher court for disposition. For a court of first instance, equally divided on the merits, to attempt to dispose of the matter one way or the other amounts to a decision of the case by less than a majority of the court. (21 *C.J.S.* 296).

In *Re First Congressional District Election,* 295 Pa. 1, 144 Atl. 735, 739, it was held:

> "When a legal or semi-legal tribunal consists of only two members, neither one of them can perform an affirmative act changing or which may change an existing condition; for it takes a majority of the whole body to do this and one is not a majority of two. It is a universal rule that when a judicial or semi-judicial body is equally divided, the subject matter with which it is dealing must remain in statu quo."

See also: *Deglow v. Kruse,* 57 Ohio St. 434, 49 N.E. 477; *In re Kings Co. E. R. Co.* (1879) 78 N.Y. 383, 385.

The rule differs in this respect from the rule on appeal where a judicial decision having once been rendered, it is proper for the Appellate Court, being equally divided in opinion, to affirm the judgment. However, even in this situation it has been the practice of this Court, where a change in the personnel of the Court is in contemplation, to grant a rehearing, so that the appeal may be disposed of on the merits. See *Commercial Molasses Corp. v. New York Tank Barge Corporation,* 313 U.S. 596; *New York, Chicago & St. Louis R. Co. v. Frank,* 313 U.S. 596; *Toucey v. New York Life Ins. Co.,* 313 U.S. 596; *Gray v. Powell,* 313 U.S. 596; *Baltimore & Ohio R. Co. v. Kepner,* 313 U.S. 597; *Bernards v. Johnson,* 313 U.S. 597; *Lisenba v. California,* 313 U.S. 597; *Reitz v. Mealey,* 313 U.S. 597.

There is an existing vacancy in the court below, and it may be assumed that in due time this vacancy will be filled. The writ should be granted in order that the review contemplated in the Act may be had, and the important questions settled by this Court, or the Court may desire as an alternative to remand the case to the court below for further consideration when the vacancy in that court shall be filled.

CONCLUSION

Petitioner has not had the review of the Commission's order which the Act provides. The court below, in affirming by an equal division, leaves outstanding an opinion by the majority of the court on the first hearing which is obviously erroneous and which we are entitled to assume constituted the basis of the ac-

tion by the three judges who voted to affirm. On the other hand, the opinion by Judge Garrecht, concurred in by Judge Mathews, and which we must assume also expresses the view of the third judge on the equal division, now has only the status of a dissenting opinion. This opinion makes manifest the errors in the Commission's interpretation and application of the statute, and the absence of substantial evidence to sustain the Commission's order.

We submit that this Court should grant the writ, and thus not only afford Petitioner the review which the Act contemplates, but also settle the important questions regarding the interpretation and application of this important Federal statute which are involved in this case.

Respectfully submitted,

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April 2, 1944,
San Francisco.

(APPENDIX FOLLOWS)

Appendix

AN ACT

To provide for control and regulation of public-utility holding companies, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Public Utility Act of 1935".

TITLE I—CONTROL OF PUBLIC-UTILITY HOLDING COMPANIES

NECESSITY FOR CONTROL OF HOLDING COMPANIES

SECTION 1. (a) Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not suscepti-

ble of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.

(b) Upon the basis of facts disclosed by the reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session), the reports of the Committee on Interstate and Foreign Commerce, House of Representatives, made pursuant to H. Res. 59 (Seventy-second Congress, first session) and H. J. Res. 572 (Seventy-second Congress, second session) and otherwise disclosed and ascertained, it is hereby declared that the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be adversely affected—

(1) when such investors cannot obtain the information necessary to appraise the financial position or earning power of the issuers, because of the absence of uniform standard accounts; when such securities are issued without the approval or consent of the States having jurisdiction over subsidiary public-utility companies; when such securities are issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties and upon the basis of paper profits from intercompany transactions, or in anticipation of excessive revenues from subsidiary public-utility companies; when such securities are issued by a subsidiary public-utility company under cir-

cumstances which subject such company to the burden of supporting an overcapitalized structure and tend to prevent voluntary rate reductions;

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public-utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

(3) When control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment;

(4) when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties; or

(5) when in any other respect there is lack of economy of management and operation of public-utility companies of lack of efficiency and adequacy of service rendered by such companies, or lack of effective public regulation, or lack of economies in the raising of capital.

(c) When abuses of the character above enumerated become persistent and wide-spread the holding com-

pany becomes an agency which, unless regulated, is injurious to investors, consumers, and the general public; and it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce; and for the purpose of effectuating such policy to compel the simplification of public-utility holding-company systems and the elimination therefrom of properties detrimental to the proper functioning of such systems, and to provide as soon as practicable for the elimination of public-utility holding companies except as otherwise expressly provided in this title.

DEFINITIONS

SEC. 2. (a) When used in this title, unless the context otherwise requires—

* * * * * * *

(7) "Holding company" means—

(A) any company which directly or indirectly owns, controls, or holds with power to vote, 10 per centum or more of the outstanding voting securities of a public-utility company or of a company which is a holding company by virtue of this clause or clause (B), unless the Commission, as hereinafter provided, by order declares such company not to be a holding company; and

(B) any person which the Commission determines, after notice and opportunity for hearing,

directly or indirectly to exercise (either alone or pursuant to an arrangement or understanding with one or more other persons) such a controlling influence over the management or policies of any public-utility or holding company as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this title upon holding companies.

The Commission, upon application, shall by order declare that a company is not a holding company under clause (A) if the Commission finds that the applicant (i) does not, either alone or pursuant to an arrangement or understanding with one or more other persons, directly or indirectly control a public-utility or holding company either through one or more intermediary persons or by any means or device whatsoever, (ii) is not an intermediary company through which such control is exercised, and (iii) does not, directly or indirectly, exercise (either alone or pursuant to an arrangement or understanding with one or more other persons) such a controlling influence over the management or policies of any public-utility or holding company as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon holding companies. The filing of an application hereunder in good faith by a company other than a registered holding company shall exempt the applicant from any obligation, duty, or liability

imposed in this title upon the applicant as a holding company, until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. As a condition to the entry of any order granting such application and as a part of any such order, the Commission may require the applicant to apply periodically for a renewal of such order and to do or refrain from doing such acts or things, in respect of exercise of voting rights, control over proxies, designation of officers and directors, existence of interlocking officers, directors and other relationships, and submission of periodic or special reports regarding affiliations or intercorporate relationships of the applicant, as the Commission may find necessary or appropriate to ensure that in the case of the applicant the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. The Commission, upon its own motion or upon application of the company affected, shall revoke the order declaring such company not to be a holding company whenever in its judgment any condition specified in clause (i), (ii), or (iii) is not satisfied in the case of such company, or modify the terms of such order whenever in its judgment such modification is necessary to ensure that in the case of such company the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. Any action

of the Commission under the preceding sentence shall be by order.

(8) "Subsidiary company" of a specified holding company means—

(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and

(B) any person the management or policies of which the Commission, after notice and opportunity for hearing, determines to be subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies.

The Commission, upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) either

through one or more intermediary persons or by any means or device whatsoever, (ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company of such specified holding company until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. As a condition to the entry of, and as a part of, any order granting such application, the Commission may require the applicant to apply periodically for a renewal of such order and to file such periodic or special reports regarding the affiliations or intercorporate relationships of the applicant as the Commission may find necessary or appropriate to enable it to determine whether in the case of the applicant the conditions specified in clauses

(i), (ii), and (iii) are satisfied during the period for which such order is effective. The Commission, upon its own motion or upon application, shall revoke the order declaring such company not to be a subsidiary company whenever in its judgment any condition specified in clause (i), (ii), or (iii) is not satisfied in the case of such company, or modify the terms of such order whenever in its judgment such modification is necessary to ensure that in the case of such company the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. Any action of the Commission under the preceding sentence shall be by order. Any application under this paragraph may be made by the holding company or the company in respect of which the order is to be entered, but as used in this paragraph the term "applicant" means only the company in respect of which the order is to be entered.

* * * * * * *

POWER TO MAKE PARTICULAR EXEMPTIONS REGARDING HOLDING COMPANIES, SUBSIDIARY COMPANIES, AND AFFILIATES

SEC. 3. (a) The Commission, by rules and regulations upon its own motion, or by order upon application, shall exempt any holding company, and every subsidiary company thereof as such, from any provision or provisions of this title, unless and except insofar as it finds the exemption detrimental to the public interest or the interest of investors or consumers, if—

(1) such holding company, and every subsidiary company thereof which is a public-utility company from which such holding company derives, directly or indirectly, any material part of its income, are predominantly intrastate in character and carry on their business substantially in a single State in which such holding company and every such subsidiary company thereof are organized;

(2) such holding company is predominantly a public-utility company whose operations as such do not extend beyond the State in which it is organized and States contiguous thereto;

(3) such holding company is only incidentally a holding company, being primarily engaged or interested in one or more businesses other than the business of a public-utility company and (A) not deriving, directly or indirectly, any material part of its income from any one or more subsidiary companies, the principal business of which is that of a public-utility company, or (B) deriving a material part of its income from any one or more such subsidiary companies, if substantially all the outstanding securities of such companies are owned, directly or indirectly, by such holding company;

(4) such holding company is temporarily a holding company solely by reason of the acquisition of securities for purposes of liquidation or distribution in connection with a bona fide debt previously contracted or in connection with a bona fide arrangement for the underwriting or distribution of securities; or

(5) such holding company is not, and derives no material part of its income, directly or indi-

rectly, from any one or more subsidiary companies which are, a company or companies the principal business of which within the United States is that of a public-utility company.

(b) The Commission, by rules and regulations upon its own motion, or by order upon application, shall exempt any subsidiary company, as such, of a holding company from any provision or provisions of this title, the application of which to such subsidiary company the Commission finds is not necessary in the public interest or for the protection of investors, if such subsidiary company derives no material part of its income, directly or indirectly, from sources within the United States, and neither it nor any of its subsidiary companies is a public-utility company operating in the United States.

(c) Within a reasonable time after the receipt of an application for exemption under subsection (a) or (b), the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of such application. The filing of an application in good faith under subsection (a) by a person other than a registered holding company shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a holding company until the Commission has acted upon such application. The filing of an application in good faith under subsection (b) shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company until the Commission has acted upon such appli-

cation. Whenever the Commission, on its own motion, or upon application by the holding company or any subsidiary company thereof exempted by any order issued under subsection (a), or by the subsidiary company exempted by any order issued under subsection (b), finds that the circumstances which gave rise to the issuance of such order no longer exist, the Commission shall by order revoke such order.

(d) The Commission may, by rules and regulations, conditionally or unconditionally exempt any specified class or classes of persons from the obligations, duties, or liabilities imposed upon such persons as subsidiary companies or affiliates under any provision or provisions of this title, and may provide within the extent of any such exemption that such specified class or classes of persons shall not be deemed subsidiary companies or affiliates within the meaning of any such provision or provisions, if and to the extent that it deems the exemption necessary or appropriate in the public interest or for the protection of investors or consumers and not contrary to the purposes of this title.

* * * * * * *

COURT REVIEW OF ORDERS

SEC. 24(a) Any person or party aggrieved by an order issued by the Commission under this title may obtain a review of such order in the circuit court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court,

within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any member of the Commission, or upon any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recom-

mendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347).

(b) The commencement of proceedings under subsection (a) shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

* * * * * * *

United States Circuit Court of Appeals
For the Ninth Circuit

No. 9918

PACIFIC GAS AND ELECTRIC COMPANY,
Petitioner,

vs.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

Upon Petition to Review an Order
of the Securities and Exchange Commission

OPINION AND DISSENTING OPINION

Before: GARRECHT, HANEY and STEPHENS,
Circuit Judges.

HANEY, Circuit Judge.

The present cause arises on a petition to review and modify, or set aside an order of the Securities and Exchange Commission.

Pacific Gas and Electric Company, petitioner, hereafter called the company, is a California corporation, and was organized in 1905. On March 23, 1912, the Public Utilities Act of California became effective, and since that date, the company could issue securities only with the approval of the Railroad Commission of California. All its securities now outstanding, have been authorized by the Railroad Commission except

15% of its common stock which was issued prior to March 23, 1912. All the company's public utility properties are located in, and its business is conducted in, the State of California.

The Public Utility Holding Company Act of 1935, hereafter called the act, became effective on August 26, 1935. Section 2(a) (8) of the act defines a "subsidiary company" as meaning:

> "(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company * * * unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and
>
> "(B) any person the management of policies of which the Commission after notice and opportunity for hearing, determines to be subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this chapter upon subsidiary companies of holding companies.
>
> "The Commission upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with

one or more other persons) either through one or more intermediate persons or by any means or device whatsoever, (ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this chapter upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this chapter upon the applicant as a subsidiary company of such specified holding company until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application."

Section 79f makes it unlawful for a subsidiary company of a registered holding company to issue or sell any of its securities except with the approval of the Commission.

On November 29, 1935, the company filed an application with the Commission for an order declaring that it was not a subsidiary company of The North American Company, a registered holding company

under the act which has held 17.71% of the company's voting stock since June 12, 1930. On September 4, 1940, the Commission directed a hearing upon such application, and on October 10, 1940, directed that such hearing commence, and it did commence, on November 12, 1940. The hearing concluded on January 16, 1941. The trial examiner on April 22, 1941, filed his report recommending that the company's petition be granted.

On July 1, 1941, the California Railroad Commission authorized the company to issue and sell 400,000 shares of its 5% First Preferred Stock, and it commenced to sell them after July 8, 1941.

On September 10, 1941, the Commission entered an order denying the company's application. At that time the company had sold 199,433 shares of the stock above mentioned. On September 18, 1941, the company filed a petition in this court to Review and Modify or Set Aside the order of the Commission, and for a stay pending such review. On the same date it filed an affidavit in support of the stay. On the following day, this court made an ex parte order staying and suspending the order and the "operation" thereof, reciting "that by Section 24 of the Public Utility Holding Company Act of 1935 said petitioner is entitled to a review of said order, and that the Court may stay the operation of said order pending review thereof".

On October 17, 1941, the Commission moved to vacate so much of the order of September 19, 1941, as provided for the stay and suspension, on four

grounds: (1) the Commission's order is not susceptible of being stayed, because of the fact, the company is a subsidiary company, and to stay the order is to have no effect other than to leave the company in the status in which the statute places it, i.e., a subsidiary company; (2) if effective to remove the company from its status as a subsidiary, the stay does not preserve the status quo because when the Commission acted, the company was a subsidiary company under the act, and a stay could not change it; (3) no great or irreparable loss or injury will be suffered by the company, if the stay is vacated, but if not, the national public interest and the interests of investors and consumers may be adversely affected; and (4) this court was without jurisdiction to stay the Commission's order because the jurisdiction to stay is for the purpose of preserving the status quo, but here, status quo, i.e., as a subsidiary company, is preserved without the stay.

Upon the hearing of respondent's motion the cause was set for hearing on the merits, and the motion taken under advisement. In view of our decision on the merits, the motion has become moot.

The Commission held that the Trial Examiner had reached his recommendation because he had misconstrued the statute. The Commission construed §2(a)(8) of the act as meaning (1) that the applicant had the burden of proving that its management and policies are not subject to the controlling influence of North American; and (2) that "controlling influence" meant something less in the form of influence on the

management or policies of a company than "control" of such company, that "control" includes the power to control, and "subject to a controlling influence" includes susceptibility to domination. It found that petitioner "has not demonstrated that its management and policies are not subject to the controlling influence of North American * * *" The two rules of law mentioned above and the finding are challenged here.

As to the finding, petitioner contends, as the Board found "that the record does not reveal any past attempts by North American to interfere affirmatively with the management or policies of P. G. & E." If petitioner's contention regarding the second rule of law above mentioned is correct, then reversal follows. However, if the Commission's view on the second rule of law is correct, then the question arises as to whether there is any substantial evidence to support the finding.

Section 2(a) (8) of the act provides that the Commission shall declare that an applicant is not a subsidiary company, if it finds three facts: (1) that the applicant is not controlled directly or indirectly by a subsidiary company; (2) that the application is not the medium of control of another company by a holding company; and (3) that "the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company * * *" so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the

obligations, duties, and liabilities imposed in this chapter upon subsidiary companies of holding companies. Since the statute requires findings of all three facts, in order to exempt a subsidiary as such, and since the third fact was not found by the Commission, the company is not entitled to exemption if the Commission's action regarding the third fact is sustained here.

The company contends that the language of the statute describing the third fact means "actual and existing control", rather than "susceptibility to control" as the Commission held, and since the Commission found that the evidence affirmatively showed a lack of actual and existing control, an exemption order should have been granted. The company quotes a portion of a committee report, and a part of Senator Wheeler's argument in the debates on the act. While the report sheds no light on the present question, the portion of the argument mentioned definitely supports the company's view. We think such argument must be disregarded because contrary to the plain meaning of the act. Penna. R. R. Co. v. International Coal Co., 230 U.S. 184, 198-199. If the company's argument were adopted, then the first and third facts enumerated in the statute would be identical, and the third would therefore be surplusage. In view of the rule, that a legislative body is presumed to have used no superfluous words in a statute (Platt v. Union Pac. R. Co., 99 U.S. 48, 58), and the rule that "effect shall be given to every clause and part of a statute" (Ginsberg & Sons v. Popkin, 285 U.S. 204, 208) we think the construction of the statute by the Commis-

sion which gives effect to the entire statute is correct and must be sustained.

We are thus brought to the questions regarding the findings and the evidence. The Commission found that the company had not "demonstrated" a lack of susceptibility to control by North American. The company argues that the Commission thus saddled it with a burden of proof to a clear and convincing degree. The Commission argues that the company has the burden of proving the lack of susceptibility to control. Dispute between the parties exists with respect to the question as to whether the statute creates a rebuttable presumption that the company is a "subsidiary company" or whether the company is "prima facie" such a subsidiary.

The words "burden of proof" are used in two senses: (1) the duty to prove a charge by a degree of proof such as a preponderance of the evidence; and (2) the duty to go forward with the evidence. Department of Water and Power v. Anderson, 9 Cir., 95 F(2d) 582, 583. In the first sense, "burden of proof" has no application to an administrative proceeding such as this. The statute does not specify any degree of proof required for any particular finding. The statute in question permits an application to be granted without hearing, but requires "notice and opportunity for hearing" if the application is denied or otherwise disposed of.

The statute does not even specify the party who shall have the duty of opening and closing the hearing. If such a hearing is held, it is only commonsense

which requires the company to present its evidence, since it seeks a particular declaration. When the evidence is all in, the Commission considers the whole body of evidence, both pro and con, and finds what the ultimate facts are unrestrained by any rule regarding burden of proof, as used in the first sense. The sole restraining rule is that the fact found must be supported by substantial evidence, as is provided in §24(a) of the act, and if such fact is so supported, it is conclusive, whether it is supported by what someone other than the Commission thinks is a *preponderance* of the evidence or not.

Since the company is, by the terms of the act, a "subsidiary" company and can be relieved of that status only by an order of the Commission, and since such an order may be made only when the Commission finds three facts, in a broad sense, it is natural to say that the company has the "burden of proof". However, when those words are used, neither of the technical senses, mentioned above, is intended. What is meant is that the company must present substantial evidence which convinces the Commission as to the three facts mentioned. We do not understand that anything different was meant in Securities and Exchange Com'n v. Sunbeam Gold M. Co., 9 Cir., 95 F(2d) 699, 702 and Detroit Edison Co. v. Securities Exchange Commission, 6 Cir., 119 F(2d) 730, 739.

The company contends that the finding of the Commission that the company "has not demonstrated that its management and policies are not subject to the controlling influence of North American" is not sus-

tained by substantial evidence. The Commission relied on facts and made inferences to support its finding, as follows:

(a) North American owns 17.71% of the voting stock in petitioner. The second largest stockholder holds 1.72% of the voting stock. The rest of the stock is owned by corporations and individuals, scattered widely. Of the total voting stock 47.9% is held by non-residents. The Commission said:

> "* * * It is apparent that if a vital and substantial conflict arose between applicant and North American and matters came to the point of a proxy fight, the holdings of North American represent a tremendous advantage in any such fight. Counsel have argued as to the possible outcome of such a proxy fight. We need not speculate here as to whether North American's 17.71% of voting power, plus the votes it could attract be offset by the voting power which the local management could attract. It cannot be denied that, in any event, North American's holdings would make it a formidable opponent. And the mere fact that there is a strong possibility that North American could prevail would, in itself, be a potent tool in influencing the management to give heed to North American's wishes."

(b) North American's holdings have represented from 25% to 30% of the total votes cast at stockholders' meetings from 1931-1940. The Board said:

> "* * * First, so long as North American is satisfied with the present management, North American's voting power and the proxy machinery in the hands of the management make it virtually

impossible for any other interest or group of interests to elect a majority of the directors. Second, North American's votes have represented 25 to 30% of the votes cast at stockholders' meetings, and, by virtue of its stockholdings, North American had the power to break a quorum at all but two stockholders' meetings since it became applicant's largest stockholder; if it had chosen to do so, no business could have been transacted at such meetings. Third, the ownership of virtually ⅓ of applicant's common stock gives North American an effective veto power over any corporate action requiring the consent of ⅔ of each class of stock —e.g., mergers and consolidations."

(c) Petitioner was organized in 1905 and now represents the consolidation of over 400 separate companies. It formerly purchased power from Great Western Power Company, which was organized in 1906. During most of the latter's existence, 90% of its revenues came from territory in competition with petitioner. Several unsuccessful attempts were made by petitioner to acquire the properties of Great Western between 1911 and 1925. Petitioner's present president is one Black, formerly an employee of Great Western. North American acquired control of Great Western in 1925, and, in 1927, Black went to New York as vice president of North American—his principal duties at that time being to keep in touch with and assist Great Western and its subsidiaries.

In 1930, following negotiations begun in the previous year between Black and petitioner's then president, resulted in the acquisition by petitioner of the

securities held by North American in Great Western and its subsidiaries. It was orally agreed that North American would not interfere with petitioner's management, that North American would be entitled to three members on petitioner's board of directors and one member on its executive committee. Black became a member of petitioner's board of directors as North American's representative.

Regarding these facts, the Commission said:

> "It is wholly untrue to characterize North American's relationship to P. G. & E. as merely that of a stockholder holding an investment interest. It now has two of its representatives on P. G. & E.'s board of directors, and by cumulating its votes it could elect at least three directors. Moreover, under the agreement made at the time of the Western Power Deal, it could at any time have a representative elected to applicant's executive committee. Against the background of the other facts we have discussed, the fact that North American has been given the 'right' to such representation on applicant's board of directors and executive committee is, we think, of material significance. We find some significance, too, in the frequent and detailed reports of every phase of applicant's operations sent by applicant to North American; no such reports are sent to any other stockholder."

(d) Regarding the facts mentioned under (c), the Commission said:

> "Nor can we disregard the fact that applicant's most important executive officer, Black, its president, was, for eight years just prior to his ap-

pointment, a senior executive of North American. From February 1927 to June 1930 Black's primary duty as vice president of North American was to exercise holding company supervision over the activities of the subsidiaries of Western Power Corporation. He conducted the negotiations for North American in which Western Power was transferred to P. G. & E. and as a result of which North American acquired its interest in P. G. & E. For five years, from 1930 to 1935, Black was the individual in the North American organization who, more than any other one person, kept advised as to applicant's business and followed applicant's affairs in the light of North American's interest. It is also significant that since Black became president of P. G. & E., no effort has been made to North American to have representation in the executive committee, and no one in North American's management has followed applicant's affairs as closely as he did. It is wholly unreal to suppose that Black would be uninfluenced by these circumstances and, in his dealings with North American, would treat it as merely a large stockholder of P. G. & E."

The facts, as thus stated, are not disputed. It is contended that the inferences drawn are contrary to the evidence. Such evidence was, of necessity, opinion evidence, because the facts inferred by the Commission were events which *might* happen, not what actually happened. In other words, the evidence relied on consisted of predictions that specified events *would not* occur, and did not consist of facts that such events *could not* happen. Manifestly, the Commission was not bound to accept the predictions as facts. As said

in Labor Board v. Link-Belt Co., 311 U.S. 584, 597: "Congress entrusted the Board, not the Courts, with the power to draw inferences from the facts * * * The Board, like other expert agencies dealing with specialized fields * * * has the function of appraising conflicting and circumstantial evidence, and the weight and credibility of testimony". The rules quoted are applicable here.

Regarding the inferences made, the only question which we may consider is one of law, that is, were the inferences made reasonable? We think a reasonable man could reach the conclusion the Commission reached, and therefore the finding must be sustained.

The company also contends that the Commission did not consider other evidence which tended to show that North American had not attempted to dominate the company in the past. However, as quoted above, the Commission found specifically in accordance with such evidence. In view of what we regard as the proper construction of the words in the statute, "subject to a controlling influence", a finding for the company is not compelled by the fact that North American had not dominated the company in the past. Congress may prevent an evil from occurring, and need not wait till the damage is done before acting. Compare: Edison Co. v. Labor Board, 305 U.S. 197, 222. We think the construction of the statute approved here, carries out what we think Congress regarded as a preventive measure.

After finding that petitioner had failed to sustain its burden of showing that it was not subject to the

controlling influence of North American, the Commission held that it was necessary or appropriate in the public interest or for the protection of investors or consumers, for petitioner to be subject to the act. It stated in this connection that petitioner "is a company with stated assets of almost $800,000,000 serving in excess of 1,500,000 customers; its securities are listed and traded on national security exchanges and are owned by investors throughout the country". This finding arises by reason of §2(a) (8) of the act quoted above.

It is obvious that what is "necessary or appropriate in the public interest" is a question for the Commission to decide. Section 1(b) of the act enumerates a number of evils existing between holding companies and their subsidiaries. Section 1(c) provides in part:

> "* * * it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted to meet the problems and eliminate the evils as enumerated in this section * * *"

The company contends that this quoted provision is the standard by which the Commission is to be guided in determining what is "necessary or appropriate in the public interest" and that there is no showing of the existence of present evils, or of "such a controlling influence as would enable the holding company to bring about the evils enumerated in the Act".

We think it is unnecessary to decide this question, because of the construction of §2(a) (8). The words

"so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies", which we will refer to as the necessity clause, are such that the meaning of the entire sentence is not clear. We think there are three possible constructions of the entire sentence.

The narrowest construction of the sentence arises when the necessity clause is construed as modifying all three of the conditions mentioned in (i), (ii) and (iii), that is, e.g., that the control mentioned in (i) must be of a kind which makes it necessary or appropriate for the applicant to be held to be subject to the act. The Commission, in In the Matter of Wisconsin Valley Improvement Company ..... S.E.C. ....., found that the applicant was subject to the controlling influence of holding companies, but that because of "the character of applicant's business and the nature and extent of statutory and state commission regulation" it was not necessary or appropriate to make the act applicable to the applicant. That decision cannot be said to be unreasonable. It seems as reasonable to say that there might be actual control under (i) and yet the same factors would prevent the control from being exercised.

A second, and more liberal construction, insofar as it gives the Commission broader powers, arises when the necessity clause is considered as modifying only the condition mentioned in (iii). In other words, if

there is control, specified in (i) or applicant is the intermediary through which such control is exercised, then the application should be denied, regardless of whether such control makes it necessary or appropriate that the applicant be held to be subject to the act, and that it is only when the applicant is subject to a controlling influence, that there must be necessity or appropriateness in the public interest for applicant to be subject to the act. Considered superficially from the standpoint of sentence structure the second construction seems to be correct. However, even though there is no control under (i) it may be that such control cannot be exercised, or the control may be regarding a thing which could not possibly harm anyone. In either event, it seems illogical to say that the necessity clause modifies the controlling influence under (iii) but not the control under (i).

A third construction, and the one which gives to the Commission the broadest powers, arises when the necessity clause is not considered as a modifying clause at all, but as a fourth condition. As thus construed, before the application could be granted it would be necessary for the Commission to find that there was no control under (i), that applicant was not an intermediary through which such control might be exercised under (ii), that applicant was not subject to a controlling influence under (iii), and that it was not necessary or appropriate in the public interest to make the act applicable to applicant. If the contrary of any of the four conditions thus enumerated were found by the Commission, then the appli-

cation would have to be denied. In other words, if the Commission found control under (i), or that applicant was the medium of control under (ii), or that applicant was subject to a controlling influence under (iii), the application would have to be denied regardless of whether there was necessity or appropriateness under the necessity clause; on the other hand, if the Commission found that none of those three conditions were present, it could still deny the application on the ground that there was a necessity or appropriateness that the act be held to be applicable to the applicant under the necessity clause.

We believe the latter construction is correct. Congress thought that the ownership by one corporation of 10% or more of the voting securities of another sufficient to declare the latter corporation to be a subsidiary, regardless of any other factor. It became a subsidiary not because of "control", or because it was the medium of control, or because it was subject to a "controlling influence", but because of the ownership of at least 10% of its stock. Congress recognized that harm might result to the public when there was such ownership, regardless of whether any of the three factors were present. It did not make as a condition to regulation any of these three factors. It is unreasonable to say that Congress intended to exempt from regulation when those three conditions only were not present. It seems apparent that harm might result to the public when none of such factors was present—that is the harm might spring from

other factors. Such factors would be covered by the fourth condition, because of its generality.

This view is not contrary to the result of the Commission's holding above mentioned. It is inconsistent to say that A is subject to the controlling influence of B, when B is prevented from exercising it. In such event, A is not subject to a controlling influence because B cannot in fact exercise it.

The remaining portion of §2(a) (8) of the act speaks of the "conditions specified in clause (i), (ii) and (iii)". It does not say that there are only three conditions, but makes it clear that the conditions referred to are those "regarding the affiliations or intercorporate relationships". The fourth condition relates to the conditions between the subsidiary and the public.

As thus construed, the application was properly denied regardless of whether the finding under the necessity clause was sustained by substantial evidence or not.

The company suggests that some constitutional questions are involved, but it does not appear that such questions were presented to the Commission, and therefore we cannot consider them. See §24(a).

The petition to review is denied.

Circuit Judge Garrecht filed a dissenting opinion, which is found at pages 1718-1738 of the record, and which is here omitted as the substance thereof is contained in his dissenting opinion, infra, on the final disposition of the case.

United States Circuit Court of Appeals
For the Ninth Circuit

No. 9918

PACIFIC GAS AND ELECTRIC COMPANY,
Petitioner,

vs.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

ORDER AFFIRMING ORDER OF SECURITIES AND EXCHANGE COMMISSION

Order of Securities and Exchange Commission herein affirmed by an equally divided Court.

United States Circuit Court of Appeals
For the Ninth Circuit

No. 9918

PACIFIC GAS AND ELECTRIC COMPANY,
Petitioner,

vs.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

DISSENTING OPINION AND CONCURRENCE

GARRECHT, Circuit Judge, dissenting:

I dissent from the per curiam decision entered herein denying the petitioner's application, for the reasons hereinafter stated.

This cause has been pending before the court upon a rehearing en banc. Former opinions of this court herein are found in 127 F.2d 378, et seq.

The issues arise on the petition of Pacific Gas and Electric Company to review and modify or set aside an order of the Securities and Exchange Commission, which denied petitioner's application for an order, pursuant to Section 2(a) (8) of the Public Utility Act of 1935 (49 Stat. 803, 807) declaring it to be not a subsidiary of the North American Company, a registered holding company owning more than 10% of the petitioner's voting stock.

Pacific Gas and Electric Company, petitioner, in the evidence and also herein sometimes referred to as P. G. & E., is a California corporation, organized in 1905. On March 23, 1912, the Public Utilities Act of California became effective, and since that date the Company could issue securities only with the approval of the Railroad Commission of California. All its securities now outstanding, have been authorized by the said Commission except 15% of its common stock which was issued prior to March 23, 1912. All the Company's public utility properties are located in, and its business is conducted in, the State of California.

The Public Utility Act, hereinafter called the Act, became effective on August 26, 1935 (49 Stat. 803). The portions of said Act pertinent to this discussion are as follows:

> "Sec. 2(a) (8) 'Subsidiary company' of a specified holding company means—

"(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B)), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and

"(B) any person the management or policies of which the Commission, after notice and opportunity for hearing, determines to be subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies.

"The Commission, upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more persons or by any means or device whatsoever, (ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not sub-

ject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company of such specified holding company until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. * * *"

Section 6 of the Act (49 Stat. 814) makes it unlawful for a subsidiary company of a registered holding company to issue or sell any of its securities except with the approval of the Commission.

It appears that North American Company, hereinafter called North American, owns, controls and holds with power to vote, 17.71% of petitioner's outstanding voting securities and is therefore, by statutory definition, a subsidiary of North American, unless declared otherwise by the Commission. Following the provisions of the Act, petitioner, on November 29, 1935, sought by appropriate petition to bring itself within the exemptions provided in the Act by alleging

and offering to establish that (1) it is not controlled, directly or indirectly, by North American; (2 it is not an intermediary company through which control of another company is exercised; and (3) its management or policies are not subject to such a controlling influence, directly or indirectly, by North American, so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers, that it be subject to obligations, duties and liabilities imposed in the Act upon subsidiary companies.

On September 4, 1940, the Commission directed a hearing upon such application and on October 10, 1940, directed that such hearing commence. It began on November 12, 1940, and was concluded on January 16, 1941. The hearing was had before a trial examiner. Although there was no real dispute as to the facts as set forth in the trial examiner's report, both counsel for petitioner and counsel for the Commission filed with the trial examiner separate requests for specific findings.

The trial examiner on April 22, 1941, made his report and findings of fact. He found and concluded that petitioner was entitled to the order which it sought. Thereupon counsel for the Commission filed exceptions to the report, and the matter was presented to the Commission upon briefs and oral argument and thereafter on September 10, 1941, the Commission entered its order denying petitioner's application. The case was brought to this court upon petition to review and modify or set aside said order.

The Commission, in concluding its findings and opinion, said:

> "* * * we hold that applicant has not demonstrated that its management and policies are not subject to the controlling influence of North American, so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed by the Act upon subsidiary companies of holding companies.
>
> "We desire to emphasize that our holding in this respect is not to be taken to mean that any stigma is cast upon applicant or that we think that applicant is not properly regarded as a California corporation. Nor do we mean to indicate that the influence of North American necessarily is or will be improperly exercised. The only question which we have decided is that, in the circumstances of this case where the statute presumptively requires that P. G. & E. be regulated as a subsidiary of North American, the facts in the record before us do not demonstrate that P. G. & E. is entitled to be excepted from the general requirement of regulation as a subsidiary of a registered holding company."

Further, the Commission said:

> "* * * There is almost no dispute as to the facts in the case as they are set forth in the trial examiner's report and in the briefs of both counsel. The point of issue with respect to the application under Section 2(a) (8) is rather one of statutory interpretation and in this respect we

cannot agree with the conclusions reached by the trial examiner. Our reasons for this decision are as follows:

"First, it is clear that the application herein cannot be granted unless we can find that applicant has sustained the burden of demonstrating that its management and policies are not subject to the controlling influence of North American. * * *"

We call attention to the fact that the findings and conclusions of the Commission are based on inference and surmise in many instances in absolute conflict with the testimony, which was uncontradicted and not discredited. The Commission made inferences to support its findings, as follows:

North American owns 17.71% of the voting stock in petitioner. The second largest stockholder owns 1.72% of the voting stock. The rest of the stock is owned by corporations and individuals, scattered widely. Of the total voting stock 47.9% is held by non-residents. The Commission said:

"* * * It is apparent that if a vital and substantial conflict arose between applicant and North American and matters came to the point of a proxy fight, the holdings of North American represent a tremendous advantage in any such fight. Counsel have argued as to the possible outcome of such a proxy fight. We need not speculate here as to whether North American's 17.71% of voting power, plus the votes it could attract would be offset by the voting power which the local management could attract. It cannot be denied that,

> in any event, North American's holdings would make it a formidable opponent. And the mere fact that there is a strong possibility that North American could prevail would, in itself, be a potent tool in influencing the management to give heed to North American's wishes."

North American's holdings have represented from 25% to 30% of the total votes cast at stockholders' meetings from 1931-1940. The Commission said:

> "* * * First, so long as North American is satisfied with the present management, North American's voting power and the proxy machinery in the hands of the management, make it virtually impossible for any other interest or group of interests to elect a majority of the directors. Second, North American's votes have represented 25 to 30% of the votes cast at stockholders' meetings and, by virtue of its stockholdings, North American had the power to break a quorum of all but two stockholders' meetings since it became applicant's largest stockholder; if it had chosen to do so, no business could have been transacted at such meetings. Third, the ownership of virtually ⅓ of applicant's common stock gives North American an effective veto power over any corporate action requiring the consent of ⅔ of each class of stock—e.g., mergers and consolidations."

Petitioner's present president is one Black, formerly an employee of Great Western Power Company. North American acquired control of Great Western in 1925, and in 1927 Black went to New York as vice president of North American—his principal duties at

that time being to keep in touch with and assist Great Western and its subsidiaries.

In 1930, following negotiations begun in the previous year between Black and petitioner's then president, the petitioner acquired the securities held by North American in Great Western Power Company and its subsidiaries. It was orally agreed that North American would not interfere with petitioner's management, that North American would be entitled to three members on petitioner's board of directors and one member on its executive committee. Black became a member of the petition's board of directors as North American's representative. Regarding these facts, the Commission said:

> "It is wholly untrue to characterize North American's relationship to P. G. & E. as merely that of a stockholder holding an investment interest. It now has two of its representatives on P. G. & E.'s board of directors, and by cumulating its votes it could elect at least three directors. Moreover, under the agreement made at the time of the Western Power Deal, it could at any time have a representative elected to applicant's executive committee. Against the background of the other facts we have discussed, the fact that North American has been given the 'right' to such representation on applicant's board of directors and executive committee is, we think, of material significance. We find some significance, too, in the frequent and detailed reports of every phase of applicant's operations sent by applicant to North American; no such reports are sent to any other stockholder."

Further, the Commission said:

> "Nor can we disregard the fact that applicant's most important executive officer, Black, its president, was, for eight years just prior to his appointment, a senior executive of North American. From February 1927 to June 1930 Black's primary duty as vice president of North American was to exercise holding company supervision over the activities of the subsidiaries of Western Power Corporation. He conducted the negotiations for North American in which Western Power was transferred to P. G. & E. and as a result of which North American acquired its interest in P. G. & E. For five years, from 1930 to 1935, Black was the individual in the North American organization who, more than any other one person, kept advised as to applicant's business and followed applicant's affairs in the light of North American's interest. It is also significant that since Black became president of P. G. & E., no effort has been made by North American to have representation in the executive committee, and no one in North American's management has followed applicant's affairs as closely as he did. It is wholly unreal to suppose that Black would be uninfluenced by these circumstances, and, in his dealings with North American, would treat it as merely a large stockholder of P. G. & E."

Admittedly, P. G. & E. is not controlled by North American and is not an intermediary company, therefore clauses (i) and (ii) of Section 2(a) (8) of the Act are not here involved. The only issues arising under clause (iii), which requires petitioner to show

that "the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company * * * as to make it necessary or appropriate in the public interest * * * that the applicant be subject to the obligations, duties, and liabilities imposed in this title * * *." Although the initial burden is on petitioner to prove to the Commission that its management and policies are not subject to North America's "controlling influence", the Commission's function is to draw adequate and fair inferences from the evidence. This the Commission failed to do.

It is an admitted fact that petitioner's utility properties are all located, and its business is conducted in the state of California. In this regard the Commission said: "On the basis of the record before us we find that applicant and all of its subsidiary companies are predominantly intrastate in character and carry on their business in California, the state in which each of them is organized, and that applicant is predominantly a public utility company whose operations as such do not extend beyond the State of California. * * *"

Petitioner is subject to the public utilities act of said state and can issue securities only with the approval of the California Railroad Commission. This state commission by its representatives appeared at the hearing and presented a statement, which was received by the Commission, showing the manner and extent of its regulation of appellant, and in this document the California Railroad Commission stated that

it was "aware of no instance during the course of this Commission's regulation of Pacific Gas and Electric Company when its management or policies appear to have been either controlled or influenced by North American Company.

While the Commission concedes that the evidence shows there is no control of petitioner by North American, the Commission maintains that it may still deny petitioner's application upon the assumption or supposition that merely ownership of 17.71 percent of the stock of petitioner by North American renders it subject to the controlling influence of such holding company despite the fact that there never has been any exercise of control or any effort in that direction and in the face of the evidence of the officers of North American that it holds the stock as an investment only and that there is no intention to exercise any control over petitioner and the further evidence of the officers and management of petitioner that they would not permit such control.

The Question of Control

Referring to the question of control as indicated by stock ownership, the court in Electric Bond & Share Co. v. Sec. & Exch. Com., 2 Cir., 92 F.2d 580, 592, said:

> "* * * Congress elected the element of stock ownership, a factor most usually indicative of control, as prima facie evidence of control. The burden of proof, which is cast upon the utility company to prove otherwise, is not onerous. Judi-

> cial review is provided to guard against any arbitrary action on the part of the Commission and to afford a remedy should the Commission's finding be not supported by substantial evidence. * * *"

That case was subsequently affirmed by the Supreme Court of the United States under the same title, 203 U.S. 419. In the latter case the Department of Justice, for the Securities and Exchange Commission, filed an able and carefully prepared brief, discussing various sections of the Act. Upon the subject of stock control, because of the clearness of the reasoning and aptness of application to the present discussion, I quote from the brief the following (Br. for Resp., p. 6, of Apx. A):

> "A holding company by express definition * * * is a company which actually controls operating companies, and not a company which merely has an investment in operating companies. Conversely, a subsidiary company, by express definition * * * is a company actually controlled by the holding company, and not simply a company in which the holding company has a substantial interest. Ten percent voting stock ownership creates a presumption of control in order to facilitate administration of the Act and to prevent ready evasion. That presumption, however, can readily be rebutted by either the putative holding company or the putative subsidiary company (Section 2(a) (7) and (8)) upon a showing that the company does not in fact exercise control. * * * No true investment company—i.e., a company which does not control the operating companies in which it invests—is in any manner affected by it."

The following quotation is also from that brief (Br. for Resp., pp. 197-198):

> "* * * a company may readily prove if such be the fact that it does not possess control. Such burden of proof is not onerous because every company has completely within its own organization full knowledge and control of all the facts and the evidence * * * Judicial review is provided to guard against any arbitrary action on the part of the Commission, and to afford a remedy should the Commission's findings of fact be not supported by substantial evidence (Section 24(a)). * * *"

With these declarations of the court and from the Commission in mind let us have a look at the testimony as found in the record and which was not contradicted.

The present board of directors consists of five directors who are officers and full-time employees of petitioner, eight directors who are prominent San Francisco business men, and two directors, Fogarty and Freeman, who are admittedly representatives of North American. Neither of these two North American representatives is a member of the executive committee.

All directors and principal officers, with the exception of the two directors who are officers of North American, are residents of San Francisco and vicinity; were either born in California or came to California early in life and have resided in California since that time; are prominently identified with Cali-

fornia enterprises, and have no substantial interest in any eastern concern, business or corporation whose business is not principally conducted in California. During the entire period of petitioner's existence the members of the board of directors, with few exceptions, have been residents of San Francisco and vicinity, and have owned and do own and represent substantial stock interests in petitioner, and the fathers of four directors (directors C. O. G. Miller, Norman B. Livermore, A. E. Wishon and W. W. Crocker) were active in the affairs of predecessor companies. All of the directors, with the exception of Fogarty and Freeman, know each other well, some are associated together in other enterprises, and several have known each other from boyhood.

The directors, other than those who are active executives of the Company, and excepting Fogarty and Freeman, are prominent in other business affairs in San Francisco and vicinity; two are chairmen of boards of local banks, one is president of a third bank; all are directors of numerous corporations, including other utilities, and several are officers or trustees of educational or charitable institutions.

Each of petitioner's local directors to whom the question was propounded, namely, Messrs. Miller, McKee, Crocker, Chickering, Livermore, Coghlan, Palmer, Nichols, McIntosh, Wishon and Black, testified that it was his opinion that North American could not if it attempted to do so and its attempts were resisted by the local directors, secure sufficient

proxies to obtain a majority of the stock represented at a stockholders' meeting.

Mr. Black testified that he would oppose any attempt by North American to control or influence the management or policies of the petitioner with "every resource at my command" and that he was sure they would not be successful in a proxy fight because:

> "This company has a rather unique position in San Francisco and in California. It has been known for many years as a California company. The fact that the Great Western Power Company was controlled by an eastern company, the Western Power Corporation, was a great handicap to the Great Western Power Company in doing business here and particularly in competition with the Pacific Gas and Electric Company. I know something of that feeling. I think 48 per cent of our stock is held here in California and I think without question that stock would be almost unanimously opposed against any attempt by any eastern interest, particularly any New York holding company, to get control of the company.
>
> "Our directors are men not only who are men who own, or are able to influence very large blocks of stock directly, but they have a standing in the community and in the business world which I think would be very decisive in getting large amounts of stock proxies from holders outside of the State. I am sure that the community as a whole would be entirely on the side of the company in any such fight."

Director Fogarty, the representative of North American on the board, testified that the manage-

ment or policies of petitioner were neither directly or indirectly subject to the controlling influence of North American. Nor had that company ever attempted to influence or control the management. He also said that as a practical matter it would not be possible. Mr. Freeman, the other representative, corroborated this view. Mr. Fogarty never attended a directors' meeting. This is also true of Mr. Freeman, who has never been in California.

The testimony of all of these witnesses is not contradicted.

With the exception of Fogarty and Freeman the evidence clearly indicates that the other directors, most of whom were prominent business men of San Francisco and vicinity, were tough-fibered individuals who could not be dominated by outside influences. That was the substance of the testimony and so far as these persons are concerned this testimony admittedly is uncontradicted. In determining the question of "controlling influence" the evidence must be considered and this the Commission did not do. It was simply waived aside as of no importance whatever.

It is probably worth remarking in this connection that North American has never solicited proxies; in fact, its officers or representatives have never voted its own stock, its proxies having been sent to other stockholders. If there existed any apprehension that North American might seek proxy control, the Commission has the power to prevent North American from soliciting any proxy.

To reach the conclusion arrived at by the Commission every circumstance is viewed with a hostile eye and every instance tortured into some semblance of sinister purpose. Thus, the selection of James B. Black as president of appellant upon the unexpected death of Mr. Hockenbeamer, who had been president for many years, is pointed to as unmistakable proof of the evil influence exerted by North American, because at the time of Black's appointment he was the vice-president of North American.

It must be admitted that Black probably was as well qualified for the position as anyone anywhere; his career is altogether a notable one. His personal, professional, and administrative achievements are detailed at some length in the record, from which I summarize briefly: He came with his parents to California at the age of twelve and has lived in San Francisco and vicinity ever since, with the exception of a short period when he resided in New York and served as vice-president of North American. He was educated in the schools of Oakland and San Francisco and at the University of California, from which he was graduated in 1913 in engineering. After graduating he was employed as a service inspector by City Electric Company, then a subsidiary of Great Western operating in San Francisco. About 1915, the properties of City Electric Company were taken over by Great Western, and Mr. Black successively engaged in sales, sales engineering, and administrative work in its San Francisco division. Later he became division manager, assistant general agent and general

sales manager, and acting general manager, and in 1922 was made vice-president, general manager and a director of that company. After North American acquired control of Western Power Corporation, Mr. Black retained these positions until February, 1927, when he went to New York at the invitation of North American as one of its vice-presidents.

His selection as president of Pacific Gas and Electric Company was entirely the result of the action of the California directors of that company, many of whom were acquainted with Black's capabilities. The fact that he was a Californian, that he was familiar with some of the properties of the company, and had wide experience were deemed qualifications, and his selection met with the unanimous approval of the board of directors. No suggestion of Mr. Black's election was made by anyone in North American; his selection was not anticipated by the officers of that company, to whom it was a surprise. There is no evidence in the record indicating that North American played any part in the choice of Black as president of the petitioner, other than to consent when the California directors asked permission to offer the position to him. When Black accepted the position he assured the California directors that he would sever all connections with North American. He has never sought or received the advice, approval, or recommendations of North American or its officers on any dividend rate, salary, refinancing, or any other pending matter. There is no difference between the information received by North American or in the relations with

petitioner since Black became president and the situation existing before that time.

Not only did the Commission disregard the uncontradicted evidence substantiating that there was no "control" or "controlling influence", it also disregarded a specific and important instance revealed by the evidence which very persuasively negatived such control. At one of the meetings of the board of directors of Pacific Gas and Electric, at which the question of declaring a dividend was up for consideration, it was voted that the dividend for that year be declared at the rate of six per cent instead of the usual eight per cent. The representatives of North American requested the board to reconsider this action, but it did not accede to the request.

Notwithstanding the uncontroverted evidence to the contrary the Commission went off into the realm of speculation as to what might happen if North American should undertake to engage in a proxy fight with appellant's existing management for control, and it determined that the mere fact that there might be a strong possibility (based likewise on conjecture) that North American could prevail was itself proof of "susceptibility" to a controlling influence.

There are other instances where the Commission very frankly has interpreted the testimony of the witnesses contrary to their evidence. These interpretations, which are exaggerated into some semblance of an argument, are then designated as inferences of the Commission as to "events which might happen" but

"not what actually happened". As approving these methods the Commission quotes an excerpt from Labor Board v. Link-Belt Co., 311 U.S. 584, 597, as follows: "Congress entrusted the Board, not the Courts, with the power to draw inferences from the facts. * * * The Board, like other expert agencies dealing with specialized fields * * * has the function of appraising conflicting and circumstantial evidence, and the weight and credibility of testimony." But here there is no conflicting evidence to appraise, and as to weight and credibility of testimony it must be noted that the witnesses who testified contrary to the findings were outstanding men of affairs in California, and they were not contradicted or impeached, and no reason appears in the record why they should be discredited.

According to the Commission petitioner was required to "demonstrate" non-control or influence by North American. The Act does not require any such mathematical extreme which excludes possibility of error. 23 C.J. 9. It is sufficient if such showing is supported by substantial competent evidence which is not contradicted. Due process requires that the competent evidence adduced be fairly considered by the Commission on its merits. As was said by Justice Brandeis in speaking for the court in the Chicago Junction Case, 264 U.S. 258, 265, "The provision for a hearing implies both the privilege of introducing evidence and the duty of deciding in accordance with it. To refuse to consider evidence introduced or to make an essential finding without supporting evidence

is arbitrary action." In Morgan v. United States, 298 U.S. 468, 480, Chief Justice Hughes said:

> "* * * The requirement of a 'full hearing' has obvious reference to the tradition of judicial proceedings in which evidence is received and weighed by the trier of the facts. The 'hearing' is designed to afford the safeguard that the one who decides shall be bound in good conscience to consider the evidence, to be guided by that alone, and to reach his conclusion uninfluenced by extraneous considerations which in other fields might have play in determining purely executive action. * * *"

This court is not called upon to determine the credibility of witnesses or to reach a conclusion upon substantially conflicting facts. Indeed, no such question is presented here, since the Commission has said in its opinion that——

> "There is almost no dispute as to the facts in this case as they are set forth in the trial examiner's report and in the briefs of both counsel. The point of issue with respect to the application under Section 2(a) (8) is rather one of statutory interpretation and in this respect we cannot agree with the conclusions reached by the trial examiner",

who found that Pacific Gas is not in fact controlled by, or subject to the controlling influence of, North American.

The Commission relies strongly on Detroit Edison Co. v. Securities and Exchange Commission, 119 F2d 730; Public Service Corporation of New Jersey v.

Securities and Exchange Commission, 129 F2d 899; and Hartford Insurance Company v. Securities and Exchange Commission, 129 F2d 794. A glance at these cases will show how utterly different were the fact there presented.

In the Hartford case, 129 F2d 794, two affiliated holding companies owned 21.98 percent of the petitioner's voting stock. Not only was the president selected from one of the subsidiaries of the holding company but he frequently had advice from his former associates and secured help from the holding company's engineers in effecting changes in the petitioner's business methods. Petitioner for years submitted a preliminary draft of its annual budget to the holding company. It obtained much of the gas that it sold to its customers through some community of interest arrangement with subsidiaries of the holding company. The cost of the gas that petitioner so purchased prior to 1940 amounted to 58 percent of all its regular operating expenses.

In the Public Service Corporation of New Jersey case, 129 F2d 899, the court pointed out that the petitioner was organized pursuant to plans submitted by the holding company which not only subscribed for 25 percent of its original stock but also underwrote part of the stock issued.

Further, under contract it supplied petitioner with engineering, purchasing and general advisory service.

The president of Public Service Corporation testified that he could not have become president of the

corporation against the wishes of the holding company and that no plan of the kind contemplated in its organization could have been accomplished without the affirmative approval of the holding company. See Public Service Corp. of New Jersey v. S. & E. C. Release No. 2998, Sept. 15, 1941.

There were many other instances of interlocking relationships, indeed, the record was so replete with evidence of the participation of the holding company in Public Service Corporation affairs that the Court passing on the appeal was moved to remark, 129 F2d 901 that the evidence supporting the findings was so conclusive and the contentions of petitioner were so wholly lacking in merit as to border on the frivolous.

Probably the case the Commission most relies upon is the Detroit Edison Co. v. Securities Exchange Commission, 119 F2d 730, as this case is cited in the Commission brief not fewer than nine times.

It is submitted that the facts in the case are so different from the one before us that it cannot be considered an authority to support the action of the Commission here. In the Detroit Edison case, by agreement with two existing companies, a syndicate organized by North American acquired their stock and organized the Detroit Edison Company. Its officers and directors were all designated by North American. On behalf of its syndicate North American then offered all of the stock of the corporation and agreed to finance and furnish other assistance to the new company on certain terms. By the deal the syndicate

acquired three million dollars of Edison's first mortgage bonds and fifty thousand shares of its stock. The Edison then began operations. Thereupon the syndicate dissolved, and North American retained more than 10 per cent of petitioner's outstanding voting securities. The record shows that the North American dominated the board of directors through the years, and at the time of the hearing the majority of directors still had affiliations with North American. There were other intercompany relationships too extended to detail here, but referred to in the opinion and which had been discontinued not long before the hearing. From these facts it was concluded that in the light of Edison's origin and the unbroken continuity of North American's officers, directors, and designees on its board, and its absolute domination for many years by the parent company, it was not entitled to an order granting exemption from the statute. In summing up the situation the court said:

> "The fact that the North American Company had abandoned some of the characteristics of 'controlling influence' over the petitioner at the time of the hearing, did not require the Commission to disregard prior interrelated activities. There is no showing that its latent power to resume such control had been extinguished. The relationship is such that they may enter into similar activities in the immediate future. * * *
>
> "* * * Giving due weight to the past transactions of petitioner with the North American and the continuing opportunity for the resumption of such activities and the extent of the petitioner's

business and the widely scattered ownership of its stock, the Commission committed no error in denying petitioner exemption from the present Act." (119 F2d at pp. 739-740.)

All the evidence in the case before us shows a complete absence of such relationships and of any control throughout the period since North American became an owner of certain stock of Pacific Gas and Electric Company because of the transfer by it of certain utility properties that it had theretofore owned.

It is significant too that those incidents of relationship which are referred to as indicative of controlling influences in practically all of the decisions which have been cited to us by the Commission are notably absent in this case as the trial examiner pointed out:

"There have been no contracts between Applicant and North American or its subsidiaries except the contract dated March 29, 1930. (The agreement by which P. G. & E. acquired the properties of North American in California.)

"Neither North American nor any of its affiliates or employees has ever performed any services with or without charge, for Applicant.

"There has been no exchange of operating information between the Applicant and the admitted subsidiaries of North American.

"There have never been any intercompany loans or financial transactions between the Applicant and North American or its subsidiaries.

"All of Applicant's major acquisitions and construction projects have been and are decided

upon, budgeted and carried out within the P. G. & E. organization and entirely independent of North American at all stages.

"North American's organization has never assisted Applicant in the preparation of any Registration Statements, nor has its Secretarial Department ever assisted Applicant in any manner.

"Applicant and North American do not employ the same accountants, attorneys or engineers.

"Applicant does not employ any former officers or employees of North American, with the exception of Mr. Black, and with the exception of those who were officers or employees of acquired companies at the time of their acquisition. North American has never recommended or suggested to Applicant the employment of any person or been asked its views thereon.

"No employees of Applicant, nor of North American or of its admitted subsidiaries have ever been loaned by either to the other."

The Commission admits that the record does not reveal any past attempt by North American to interfere with its management or policies. It is likewise conceded that there is no evidence of actual control, nor, as has been shown, is there any substantial evidence from which any legally sound inference can be drawn that there ever was any effort whatsoever by North American to subject appellant to any controlling influence. Nor is there any testimony in the record from which any fair inference can be drawn that petitioner was subject to the controlling influence of North American.

SUBJECT TO A CONTROLLING INFLUENCE

Petitioner makes the point that the Act requires some present controlling influence, not a speculative future influence, as ground for denial of an application for a declaration. The term "subject to a controlling influence" means that approximately as of the time of the hearing the controlling influence must be actually existent even though not actively executed and that some mere potential or possible or speculative influence is not sufficient. The statute seems to imply such an interpretation. It reads "subject to a controlling influence". The word "subject" suggests some present existing quiescent controlling power that could be rendered active at will. This may also be inferred because in this very Section 2(a) (8) it is provided that even where the Commission has acted favorably and made an order of exception this finding of the non existence of "controlling influence" may be only conditional and temporary, and "The Commission, upon its own motion or upon application, shall revoke the order * * * whenever in its judgment such modification is necessary" to effectuate the law. These provisions indicate that the Congress intended to cover a situation where there might be some "susceptibility" of such influence in the future but where none presently existed and that it did not intend that a declaration should be withheld in the absence of present active controlling influence.

From the discussion in Congress at the time the Act was under consideration and as well from the fair and ordinary meaning of the language, the phrase

"subject to a controlling influence" does not mean, as the Commission found, that appellant was required to "demonstrate" that its management and policies were not "susceptible to control" by North American. "Subject to a controlling influence" is not the equivalent of "susceptible to a controlling influence". "Susceptible" and "subject" are not interchangeable or synonymous terms. The word "susceptible" connotes an especial liability to mental and emotional impressions. Advisedly that expression was not used in the statute. But the word "subject" is used, and here it occurs in relation with "control", and in that sense it must correctly be continued as meaning under the power or dominion of another. It is synonymous with subordinate, inferior,[1] "To control" means to exercise a restraining or direct influence over; to dominate; regulate; hence to hold from action; to curb; to subject.[2] Moreover, "controlling" means the act or fact of exercising restraining influence over, which conveys the idea of a continuing process. Thus, "subject to a controlling influence", as stated in the statute, is not the same thing as "susceptibility" to a controlling influence as expressed by the Commission. One phrase refers to an actually existing state; the other might be applied to some future condition which uncertain events might possibly bring about. In considering this aspect of the matter it is important to keep in mind that under the statute as above noted the Commission is in a position to act at once if ever

[1]See Webster's New International Dictionary.

[2]Ibid.

the susceptibility should become an actuality, even if the Commission had theretofore granted petitioner an exemption at a time when the facts showed a lack of any actual and existing control or controlling influence.

It is also clear that the vague, artificial tests here employed are not sanctioned by the Act. Nor was it expected that inferences based upon inferences, or suppositions, or even possibilities, would be substituted for substantial evidence.

The facts presented to the Commission and all reasonable inferences, deductions, and conclusions to be drawn therefrom, considered in their entirety and in relation to one another, negative the findings of the Commission. The inferences which are suggested as supporting the order of the Commission are based on mere suspicion. In Labor Board v. Columbian Co., 306 U.S. 292, 299-330, Mr. Justice Stone said:

> "* * * But as has often been pointed out, this, as in the case of other findings by administrative bodies, means evidence which is substantial, that is, affording a substantial basis of fact from which the fact in issue can be reasonably inferred. * * * Substantial evidence is more than a scintilla, and must do more than create a suspicion of the existence of the fact to be established. 'It means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion,' * * *"

In vesting the Commission with the duty of ascertaining "control" or "subject to a controlling influ-

ence" of one company by another Congress did not imply that a potential facility to exercise control was sufficient to establish such controlling influence. If this alone were sufficient the Congress would not have made provision for the exemption.

The legislative history of the Act corroborates this view. In the course of the debate on the bill, Senator Wheeler, chairman of the Committee in charge, said, with reference to the 10 percent clause (79 Cong. Rec., p. 8397):

> "That is only prima facie evidence; but even if they hold 40 percent of the stock of a company they may come before the Commission and produce evidence that they are not actually in control of the company, and the Commission is directed to make a finding and to exempt them if they are not actually controlling the company as the word 'control' is defined in the bill."

Again, Senator Wheeler said (79 Cong. Rec., p. 8439):

> "No, Mr. President. Let me make a distinction. The Senator from Delaware said: 'Suppose I own 10 percent of the stock of some company.' Unless I control that company I am not a holding company under the terms of this bill. The mere ownership of the 10 percent of the stock does not of itself make him a holding company, because unless he actually controls the company he is not a holding company. The Senator may overlook the factor of control. He may show that he actually does not control the company in

which he owns 10 percent of stock, and if he does not have control he is not a holding company."

Neither the Commission nor the Court is warranted in departing from the purposes expressed because of any doubts that may exist as to the wisdom of following the course which Congress has marked out.

There must be some substantial evidence before the Commission that there exists such a controlling influence as would enable the holding company to bring about the evils enumerated in the Act. There is no such showing in this case.

On the contrary, the evidence affirmatively shows, as the examiner in his findings pointed out, the absence of the evils which the Act was designated to prevent.

Pacific Gas and Electric Company never had any financing, purchasing, service, management, construction or similar contracts with North American or its affiliates.

North American has never had anything whatever to do with accounting practices and rate dividends and other policies of Pacific Gas and Electric Company.

There are and have been no management, service, sales, construction or other contracts in existence, nor has there been, nor is there any evidence of control or influence exerted or attempted to be exerted over Pacific Gas and Electric Company's finances, management, and policies.

Present prospective investors in Pacific Gas and Electric securities can obtain information necessary to appraise its financial condition and earning power. It issues a comprehensive annual report and keeps its accounts in accordance with a uniform system prescribed for gas and electric corporations by the California Railroad Commission, all of which are open to the public. During all the years North American has been a stockholder in the Pacific Gas and Electric Company, it has never had any transactions with Pacific Gas and Electric Company other than the original purchase from it in 1930.

There has been no increase or extension of North American's interest in Pacific Gas and Electric, and its relative voting power is less than it was immediately after it became a stockholder in 1930. The list enumerating the absence of many evils usually relied upon by the Commission in these cases is extended at length in the findings of the examiner, which have not been questioned. They are too numerous to detail here.

Moreover, under the Act the Commission now actually exercises over North American, as a registered holding company, such control as is itself sufficient to prevent the occurrence of any transaction or dealing between the companies as would violate the Act. While no such transactions have ever occurred and the evidence that they would not occur is uncontradicted, still the Commission by virtue of this control over North American can at once prevent them should they be proposed. Indeed, the Commission has already

made an order which was affirmed by the Circuit Court of Appeals for the Second Circuit, North American Company v. S. & E. C., 133 F2d 148, under which North American is required to dispose of its stock in petitioner.

To sustain the Commission on the record here would require us to hold, as the court did on the first hearing, that its determination of what is necessary in the public interest is a matter within the uncontrolled discretion of the Commission. This is not the proper interpretation of the statute and counsel representing the Commission do not so contend.

The order of the Commission not being supported by substantial evidence should be set aside.

MATHEWS, Circuit Judge, joins in this dissent.